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To the Honorable City Council and Board of Public Utilities
City of Riverside
Riverside, California

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying financial statements of the City of Riverside, California, Water Utility, an enterprise fund of the City, as of and for the year ended June 30, 2009 as listed in the table of contents. These financial statements are the responsibility of the City of Riverside Water Utility's management. Our responsibility is to express an opinion on these financial statements based on our audits. The prior year partial comparative information has been derived from the financial statements of the Water Utility for the year ended June 30, 2008 and, in our report dated October 3, 2008, we expressed an unqualified opinion on those financial statements.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the financial statements, the financial statements of the City of Riverside, California, Water Utility are intended to present the financial position and the changes in financial position and cash flows for the City of Riverside, California, Water Utility, a fund of the City, and do not purport to, and do not, present fairly the financial position of the City of Riverside, California, and the changes in its financial position and its cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Riverside, California, Water Utility, as of June 30, 2009 and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



To the Honorable City Council and Board of Public Utilities
City of Riverside
Page 2

Our audits were conducted for the purpose of forming an opinion on the financial statements that comprise the City of Riverside, California, Water Utility's basic financial statements. The supplementary information entitled Water Key Historical Data, as listed in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2009 on our consideration of the City of Riverside's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Mayer Hoffman Mc Cann P.C.

San Jose, California
October 29, 2009



MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

As management of Riverside Public Utilities (a department of the City of Riverside), we offer the readers of Riverside's Water Utility financial statements, an enterprise fund of the City, this narrative overview and analysis of the financial activities of the Water Utility (Utility) for the fiscal years ended June 30, 2009 and 2008. We encourage readers to consider the information presented here in conjunction with additional information furnished in our financial statements, which begin on page 52 of this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

FINANCIAL HIGHLIGHTS

Fiscal years 2009 and 2008 reflected strong operating results for the Water Utility, with retail sales exceeding the previous year's results, primarily from an expanded customer base and the effects of rate increases offset by a decrease in consumption.

- Retail sales, net of reserve/recovery were \$49,591 and \$46,164 for the years ended June 30, 2009 and 2008, respectively. The increase in sales was primarily due to recent rate increases to support the Water Utility's Water Master, Water Supply and Asset Management Plans, offset by a 2.5% reduction in retail consumption.
- The assets of the Water Utility exceeded its liabilities (equity) at the close of fiscal years 2009 and 2008 by \$275,143 and \$274,487, respectively. Of this amount, \$30,911 and \$37,884, respectively, may be used to meet the Utility's ongoing obligations to creditors and customers.
- The Utility's total equity as of June 30, 2009 and 2008 increased by \$656 and \$20,570 from fiscal years ended June 30, 2008 and 2007, respectively. The 2009 increase was significantly impacted by the effects of the Special Item (see Note 8).
- As of June 30, 2009 and 2008, unrestricted equity represented over 67% and 88% of annual operating expenses, respectively.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Riverside Water Utility financial statements. The Water Utility is a department of the City of Riverside, and its activities are recorded in a separate enterprise fund. These financial statements include only the activities for the City of Riverside Water Utility and provide comparative information for the last two fiscal years. Information on city-wide financial results is available in the City of Riverside's "Comprehensive Annual Financial Report."

The City of Riverside Water Utility's financial statements comprise two components: 1) financial statements, and 2) notes to the financial statements. In addition, this report also contains other supplementary information to provide the reader with additional information about the Water Utility, including key historical operating and other relevant data.

Included as part of the financial statements are three separate statements, which collectively provide an indication of the Water Utility's financial health.

The **Balance Sheets** present information on assets and liabilities, with the difference between the two reported as equity. Over time, increases or decreases in equity may serve as a useful indicator of whether the financial condition of the Utility is improving or deteriorating.

The **Statements of Revenues, Expenses and Changes in Equity** present information showing how the Utility's equity changed during the most recent two fiscal years. Results of operations are reported as underlying events occur, regardless of the timing of cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods, e.g., accounts payable and accounts receivable. This is called the accrual basis of accounting and is more fully described in the accompanying Notes to the Financial Statements.

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

The **Statements of Cash Flows** present the cash flow changes occurring during the last two fiscal years in highly liquid cash and cash equivalents, including certain restricted assets.

The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data provided in the Water Utility's financial statements. The notes to the financial statements can be found on pages 56 to 67 of this report.

UTILITY FINANCIAL ANALYSIS

As noted earlier, equity (also called net assets) may serve over time as a useful indicator of the fund's financial position. In the case of Riverside's Water Utility, assets exceeded liabilities by \$275,143 and \$274,487 at the close of the fiscal years 2009 and 2008, respectively.

The following table summarizes the Water Utility's financial condition as of June 30, 2009, 2008 and 2007:

CONDENSED STATEMENTS OF EQUITY (NET ASSETS)

	2009	2008	2007
Current and other assets	\$ 82,220	\$ 117,858	\$ 77,827
Capital assets	356,089	324,636	286,396
Total assets	438,309	442,494	364,223
Long-term debt outstanding	143,522	147,349	91,568
Other liabilities	19,644	20,658	18,738
Total liabilities	163,166	168,007	110,306
Invested in capital assets, net of related debt	237,188	230,347	208,882
Restricted	7,044	6,256	5,328
Unrestricted	30,911	37,884	39,707
Total equity (net assets)	\$ 275,143	\$ 274,487	\$ 253,917

ASSETS

Fiscal Year 2009 Total assets of \$438,309 reflect a decrease of \$4,185 (1.0%), mainly due to the following:

- Current and other assets, which comprise of restricted and unrestricted assets, reflect a net decrease of \$35,638 due to the use of \$28,284 of bonds proceeds for capital projects. Accounts receivable from other utilities and governments decreased by \$7,032 primarily due to the reduction of a receivable from the State of California for reimbursement for capital construction projects.
- The increase in net capital assets (Utility plant) of \$31,453 was a result of significant investment in the pipeline replacement program, system expansion and improvements, and construction of treatment facilities as discussed in the "Capital Assets and Debt Administration" section on page 50 of this report.

Fiscal Year 2008 Total assets of \$442,494 reflect an increase of \$78,271 (21.5%), due to a \$38,240 increase in net capital assets (Utility plant) primarily relating to the pipeline replacement program, system expansion and improvements, and construction of treatment facilities (of which approximately 50% was funded by the State of California Proposition 50 grant funds). Current and other assets reflect a net increase of \$40,031 due to the issuance of the 2008 Water Revenue Series B Bonds which resulted in an increase in bond proceeds offset by the use of bond proceeds for capital projects and a decrease in operating cash used for capital construction projects eligible for reimbursement from the State.

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

LIABILITIES

Fiscal Year 2009 The Utility's total liabilities were \$163,166, a decrease of \$4,841 (2.9%), due to the following:

- Long-term debt outstanding decreased by \$3,827 due to principal repayments, amortization of deferred bond refunding costs, capital appreciation, and bond discounts and premiums.
- Other liabilities decreased by \$1,014 primarily from a \$911 decrease in payables and accrued liabilities.

Fiscal Year 2008 The Utility's total liabilities increased by \$57,701 (52.3%) to \$168,007. Long-term debt outstanding increased by \$55,781 primarily due to the issuance of the 2008 Water Revenue Series B Bonds offset by principal repayments. Other liabilities increased by \$1,920 due to an increase in accounts payable and accrued liabilities offset by a decrease in customer deposits.

EQUITY (NET ASSETS)

Fiscal Year 2009 The Water Utility's equity, which represents the difference between the Utility's resources and its obligations, totaled \$275,143, an increase of \$656 (less than 1.0%), is comprised of the following:

- The largest portion of the Utility's equity is \$237,188 (86.2%), and reflects its investment in capital assets, such as treatment, pumping, source of supply, transmission and distribution facilities, less any related outstanding debt used to acquire those assets. This portion increased by \$6,841 (3.0%) over prior fiscal year due to the amount of capital assets constructed or purchased that were not bond financed. The Water Utility uses these capital assets to provide services to customers; consequently, these assets are not available for future spending. Resources needed to repay the outstanding debt shown on the Balance Sheets must come from other sources such as operations, since the capital assets themselves cannot be used to liquidate these long-term obligations. Additional capital asset information can be found in the "Capital Assets and Debt Administration" section.
- The restricted portion totaled \$7,044 (2.6% of total equity), and represents resources that are subject to internal and external restrictions on how they may be used. These are reserved for items such as debt repayment and funds collected for the Water Conservation and Reclamation programs. This portion increased by \$788 from prior fiscal year primarily due to increases in Water Conservation and Reclamation program assets.
- The unrestricted portion totaled \$30,911 (11.2% of total equity), a decrease of \$6,973, primarily attributable to the results of positive operations offset by the effects of the Special Item (see Note 8) and the use of unrestricted equity to fund capital projects. This portion may be used to meet the Utility's ongoing obligations to creditors and customers.

Fiscal Year 2008 Total Water fund equity increased \$20,570 (8.1%) to \$274,487. The largest portion of the equity, \$230,347 (83.9%), is represented by investment in capital assets, which increased by \$21,465 (10.3%) due to the amount of capital assets constructed or purchased that were not bond funded. The restricted portion increased by \$928 primarily due to increases in Water Conservation and Reclamation program assets. The unrestricted portion decreased by \$1,823 due to positive operating results for fiscal year 2008, offset by the use of unrestricted equity to fund capital projects and additional debt service reserves.

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

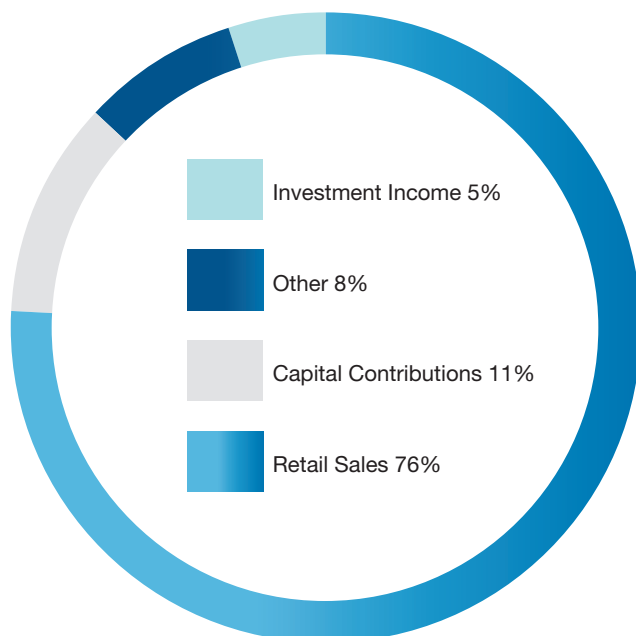
The Water Utility's overall increase in equity of \$656 and \$20,570 during fiscal years 2009 and 2008, respectively, was due to positive operating results that can be further explained in the following Condensed Statements of Changes in Equity:

CONDENSED STATEMENTS OF CHANGES IN EQUITY (NET ASSETS)

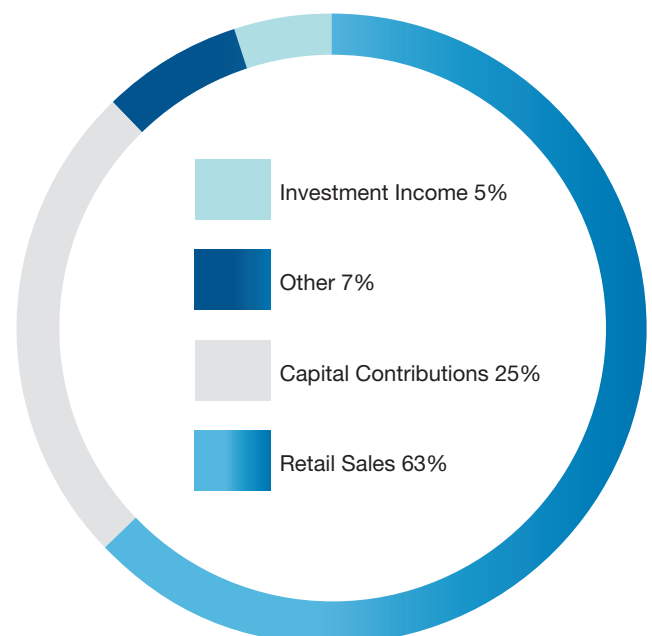
	2009	2008	2007
Revenues:			
Retail sales, net	\$ 49,591	\$ 46,164	\$ 43,403
Other revenues	5,311	5,206	4,491
Investment income	3,169	3,357	2,931
Capital contributions	7,148	18,116	20,074
Total revenues	65,219	72,843	70,899
Expenses:			
Operations and maintenance	29,678	27,795	23,449
Purchased energy and water	6,401	6,316	6,233
Depreciation	9,771	8,806	7,783
Interest expense and fiscal charges	7,049	4,401	4,469
Total expenses	52,899	47,318	41,934
Transfers to the City's general fund	(5,276)	(4,955)	(3,928)
Special item	(6,388)	-	-
Changes in equity	656	20,570	25,037
Equity, July 1	274,487	253,917	228,880
Equity, June 30	\$ 275,143	\$ 274,487	\$ 253,917

REVENUES BY SOURCES

June 30, 2009



June 30, 2008



MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

Fiscal Year 2009 Total revenues of \$65,219 decreased by \$7,624 (10.5%) from prior fiscal year, due to the following major changes:

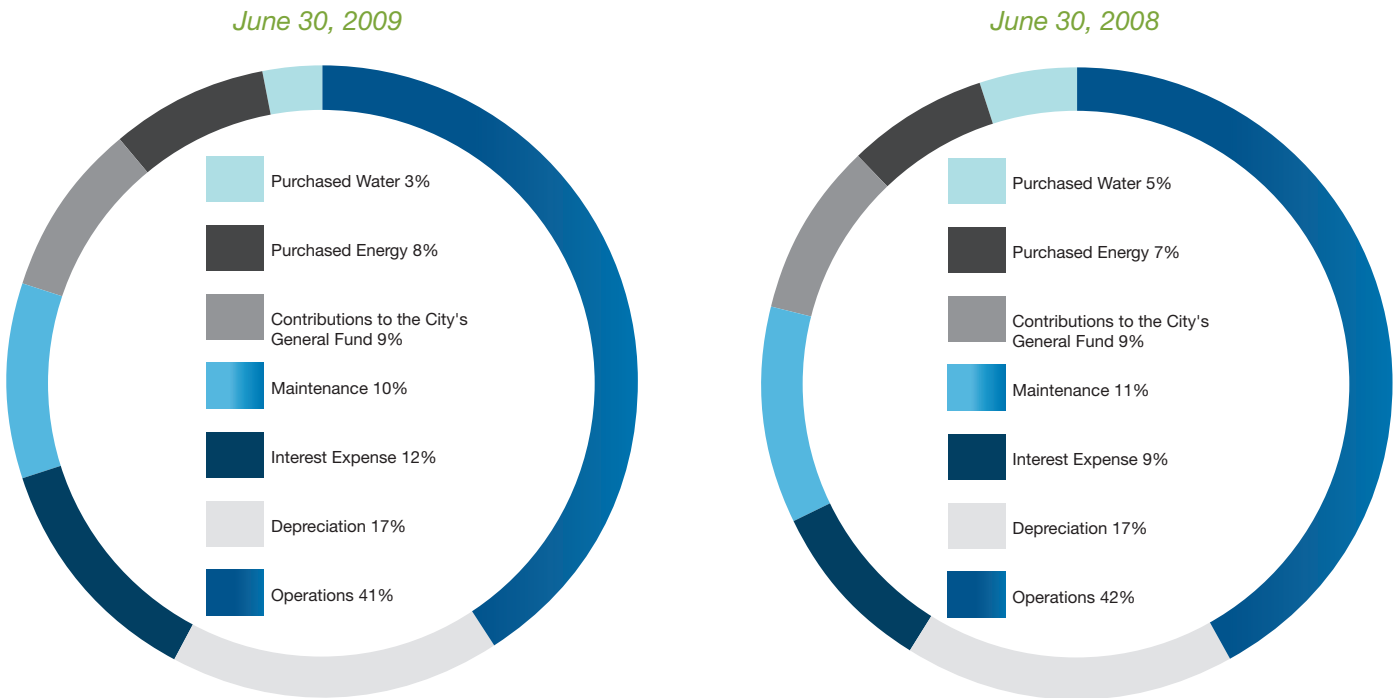
- Retail sales (residential, commercial, industrial, and other sales), net of reserve/recovery, totaled \$49,591, an increase of \$3,427 (7.4%) over the prior fiscal year. Retail sales continue to be the primary revenue source for the Water Utility, making up 76.0% of total revenues. The increase in retail sales was primarily due to a 10.0% rate increase that became effective November 1, 2008 as part of the SAFE W.A.T.E.R. Plan, offset by a 2.5% decrease in retail consumption.
- Other revenues of \$5,311 increased by \$105 (2.0%) predominantly due to an increase in wholesales sales attributed to our Wheeling agreement.
- Investment income of \$3,169 reflects a decrease of \$188 (5.6%), due to an overall decrease of \$644 in the fair market value and interest from investments, offset by an increase of \$456 on interest earned on bond construction cash.
- Capital contributions were \$7,148 and reflect a decrease of \$10,968 (60.5%), primarily due to a decrease of \$7,512 in contributions from State grants for reimbursable capital project costs, decreases of \$1,307 in non-cash developer contributions, and \$1,558 from developers for construction projects due to the slowdown in development related activities.

Fiscal Year 2008 Total revenues of \$72,843 increased by \$1,944 (2.7%) from prior fiscal year, due to the following major changes:

- Net retail sales were \$46,164, 63.3% of total revenues, reflecting an increase of \$2,761 (6.4%) in net retail sales from the prior fiscal year primarily due to a 10.0% rate increase that became effective November 1, 2007 as part of the SAFE W.A.T.E.R. Plan, offset by a 6.1% decrease in retail consumption.
- Other revenues of \$5,206 increased by \$715 (15.9%) predominantly due to gains on the sale of assets.
- Investment income of \$3,357 reflects an increase of \$426 (14.5%), primarily due to a net increase in the fair market value of investments.
- Capital contributions were \$18,116 and reflect a decrease of \$1,958 (9.8%), primarily due to an increase of \$10,047 in contributions from State grants for reimbursable capital project costs, offset by a decrease of \$6,168 in non-cash contributions for treatment facilities from settlement agreements with parties responsible for contaminating the Water Utility's ground water resources, and a decrease of \$5,837 in construction projects funded by developers.

MANAGEMENT’S DISCUSSION AND ANALYSIS: WATER

EXPENSES BY SOURCES



Fiscal Year 2009 Total expenses were \$52,899, an increase of \$5,581 (11.8%), due to the items discussed below:

- Operations and maintenance costs were \$29,678, and reflect an increase of \$1,883 (6.8%), primarily due to increases in personnel-related expenses and general operating expenses. Overall purchased energy and water costs were consistent with prior year; however, electricity costs increased \$928 due to pumping water from deeper ground levels due to ongoing drought conditions. Although the Utility did not purchase any water in the current year, it recorded \$1,823 (\$843 lower than prior year) primarily for over-pumping its entitlement in local ground water in previous years and to pay availability charges related to pumping rights.
- Interest expense and fiscal charges were \$7,049, and reflect an increase of \$2,648 (60.2%), due to a full year of interest costs associated with the 2008 Water Revenue Series B bonds.
- Depreciation expense of \$9,771 increased \$965 (11.0%) primarily due to the completion of \$45,307 of capital projects that were included as depreciable capital assets.

Fiscal Year 2008 Total expenses were \$47,318, reflecting an increase of \$5,384 (12.8%), due to an increase in personnel-related expenses, professional service costs, maintenance expenses and the cost of electricity and gas necessary for operations, offset by a reduction in purchased water costs.

TRANSFERS

Transfers to the City’s general fund are limited to a maximum of 11.5% of the prior year gross operating revenues by Section 1204(f) of the City Charter. The City uses these funds to help provide needed public services to the residents of the City, including police, fire, parks, libraries and other benefits.

Fiscal Year 2009 The Water Utility transferred the maximum allowable by the City Charter to the City’s general fund, or \$5,276, an increase of \$321, primarily the result of a \$2,761 increase in retail sales for fiscal year 2008. See also Note 8 regarding a Special Item transaction with the City’s general fund.

Fiscal Year 2008 Transfers to the City’s general fund of \$4,955 increased by \$1,027, primarily the result of increased retail sales of \$9,102 for fiscal year 2007.

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

CAPITAL ASSETS AND DEBT ADMINISTRATION

CAPITAL ASSETS

The Water Utility's investment in Capital Assets includes investments in source of supply, pumping, treatment, transmission and distribution facilities, and construction in progress, as well as general items such as office equipment, furniture, etc.

The following table summarizes the Utility's capital assets, net of depreciation as of June 30:

	2009	2008	2007
Source of supply	\$ 49,485	\$ 24,719	\$ 22,266
Pumping	13,534	11,451	7,641
Treatment	19,843	20,613	20,293
Transmission and distribution	226,454	217,071	195,557
General	5,542	5,253	3,680
Land	10,809	7,682	3,923
Intangible	6,015	5,969	5,969
Construction in progress	24,407	31,878	27,067
Total	\$ 356,089	\$ 324,636	\$ 286,396

Fiscal Year 2009 The Water Utility's investment in capital assets, net of accumulated depreciation was \$356,089, an increase of \$31,453 (9.7%). The increase resulted primarily from the following significant capital projects:

- \$6,642 for continued pipeline replacement programs.
- \$23,638 for system expansion and improvements including pump station replacements, reservoir construction and facilities rehabilitation.
- \$4,129 for completion of the John W. North Treatment facility which will greatly increase the water supply and was one of the recommended system improvements in the SAFE W.A.T.E.R. Plan.
- \$2,661 for property acquisitions for future reservoirs, booster stations and other system expansion or improvement projects (see Note 8).

Fiscal Year 2008 Investment in capital assets, net of accumulated depreciation, for the Water Utility increased \$38,240 (13.4%), for a total of \$324,636. Major capital projects included \$6,156 for continued pipeline replacement programs, \$10,768 for system expansion and improvements to water facilities, and \$20,463 for the John W. North Treatment facility.

DEBT ADMINISTRATION

The following table summarizes outstanding long-term debt (revenue bonds) as of June 30:

	2009	2008	2007
Revenue bonds	\$ 149,020	\$ 153,395	\$ 99,515
Contracts payable	949	964	974
Less:			
Current portion	(4,565)	(4,525)	(4,505)
Unamortized deferred bond refunding costs	(3,101)	(3,198)	(2,510)
Unamortized capital appreciation	(427)	(938)	(1,629)
Unamortized bond premium (discount)	1,646	1,651	(277)
Total	\$ 143,522	\$ 147,349	\$ 91,568

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

The Water Utility's bond indentures require the Utility to maintain a minimum debt service coverage ratio, as defined by the bond covenants, of 1.25. The Water Utility's debt service coverage ratio was 2.25, 3.88, and 3.38 at June 30, 2009, 2008, and 2007, respectively. The debt is backed by the revenues of the Utility (revenue bonds).

Fiscal Year 2009 Total long-term debt decreased by \$3,827 (2.6%) to a total of \$143,522, due to \$3,787 of principal repayments, amortization of deferred bond refunding costs, capital appreciation, and bond discounts and premiums.

Fiscal Year 2008 Long-term debt of \$147,349 increased by \$55,781 (60.9%), due to the May 15, 2008 issuance of the 2008 Water Revenue Series B Bonds in the amount of \$58,235, offset by \$4,364 of principal repayments, amortization of deferred bond refunding costs, capital appreciation, and bond discounts and premiums.

Additional information on the Water Utility's long-term debt can be found in Note 4 on pages 62 to 66 of this report.

CREDIT RATINGS

The Water Utility maintains an "AA+" credit rating from Standard & Poor's and "AA" from Fitch Ratings for its revenue bonds.

ECONOMIC FACTORS AND RATES

Although inflationary trends in the Riverside region continue to compare favorably to the national indices, the Water Utility's escalation in costs are not strictly attributable to inflation. One of the primary drivers of the increase in costs relates to the Water Utility's aging infrastructure.

To address this concern, in March 2006, the Board of Public Utilities, after the requisite public hearing, adopted and the City Council unanimously approved, the SAFE W.A.T.E.R. (Water Available to Everyone in Riverside) Plan. This plan implements system improvements contained in the Water Master, Water Supply and Asset Management Plans. The SAFE W.A.T.E.R. Plan is initially funded by a fifty-two percent, five-year water rate increase, consisting of a twelve percent and four-ten percent increases effective November 1, 2006, 2007, 2008, 2009, and 2010, respectively.

The Utility is impacted by the recent economic decline affecting virtually all industries in the United States, with retail consumption decreasing 2.5% and 6.1% in fiscal years 2009 and 2008, respectively, over the previous year levels. In addition, the water revenues are dependent on weather conditions, with significant wet weather years impacting revenue as residents reduce water used for outdoor landscaping.

The state has reduced water exports from northern to southern California which has significantly increased the costs for imported water. With completion of the John W. North Water Treatment Plant, Riverside is water independent and does not expect any increase costs to its customers due to the curtailment of water deliveries to Southern California. This new plant created a new source of supply and the City has executed an agreement with another local water supplier which is expected to produce additional revenue of \$1.5 to \$2.0 million per year.

In addition to inflation, management continually plans for and identifies issues or potential contingencies that could impact future rates such as reclaimed water, infrastructure needs—both locally and at the state level if such state-wide costs are ultimately passed through to all Californians, system growth, source of supply, ground water contamination, stricter contaminant guidelines, legislative mandates, and others. In an effort to control costs to its customers, the Utility is aggressive in pursuing outside parties, and holding them responsible for any negative effects they may cause to Riverside's water quality.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City of Riverside Water Utility's finances. Questions concerning any information provided in this report or requests for additional financial information should be addressed to the Assistant General Manager Finance/Customer Services, Riverside Public Utilities, 3901 Orange Street, Riverside, CA 92501. Additional financial information can also be obtained by visiting www.RiversidePublicUtilities.com.

BALANCE SHEETS: WATER

ASSETS	June 30,	June 30,
	2009	2008
	(in thousands)	
UTILITY PLANT:		
Source of supply	\$ 61,392	\$ 35,880
Pumping	20,782	18,219
Treatment	23,772	23,772
Transmission and distribution	327,189	311,288
General	13,275	12,288
	446,410	401,447
Less accumulated depreciation	(131,552)	(122,340)
	314,858	279,107
Land	10,809	7,682
Intangible	6,015	5,969
Construction in progress	24,407	31,878
	356,089	324,636
Total utility plant (Note 3)		
RESTRICTED ASSETS:		
Cash and cash equivalents (Note 2)	5,156	4,862
Cash and investments at fiscal agent (Note 2)	27,726	56,694
	32,882	61,556
Total restricted non-current assets		
OTHER NON-CURRENT ASSETS:		
Deferred pension costs	5,705	5,782
Deferred bond issuance costs	1,624	1,702
	7,329	7,484
Total other non-current assets		
Total non-current assets		
CURRENT ASSETS:		
Unrestricted assets:		
Cash and cash equivalents (Note 2)	29,679	29,577
Accounts receivable, less allowance for doubtful accounts		
2009 \$99; 2008 \$121	5,580	5,860
Accounts receivable, other utilities and governments, less allowance		
for doubtful accounts 2009 \$115; 2008 \$179	4,686	11,718
Accrued interest receivable	146	260
Prepaid expenses	7	6
	40,098	47,421
Total unrestricted current assets		
Restricted assets:		
Cash and cash equivalents (Note 2)	1,761	1,249
Conservation and Reclamation Programs receivable	150	148
	1,911	1,397
Total restricted current assets		
Total current assets		
Total assets	\$ 438,309	\$ 442,494

* See accompanying notes to the financial statements

BALANCE SHEETS: WATER

EQUITY AND LIABILITIES	June 30, 2009	June 30, 2008
	(in thousands)	
EQUITY:		
Invested in capital assets, net of related debt	\$ 237,188	\$ 230,347
Restricted for:		
Debt service (Note 5)	5,156	4,862
Conservation and Reclamation Programs	1,888	1,394
Unrestricted	30,911	37,884
Total equity	275,143	274,487
LONG-TERM OBLIGATIONS, LESS CURRENT PORTION (NOTE 4)	143,522	147,349
OTHER NON-CURRENT LIABILITIES:		
Pension obligation (Notes 1 and 4)	5,584	5,682
Postemployment benefits payable (Notes 1 and 4)	526	250
Total other non-current liabilities	6,110	5,932
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS:		
Accrued interest payable	1,156	568
Conservation and Reclamation Programs payable	23	3
Current portion of long-term obligations (Note 4)	4,415	4,375
Total current liabilities payable from restricted assets	5,594	4,946
CURRENT LIABILITIES:		
Accounts payable	5,768	6,862
Accrued liabilities	1,461	2,142
Current portion of long-term obligations (Note 4)	150	150
Customer deposits	561	626
Total current liabilities	7,940	9,780
Total liabilities	163,166	168,007
COMMITMENTS AND CONTINGENCIES (NOTES 6 AND 7)	-	-
Total equity and liabilities	\$ 438,309	\$ 442,494

* See accompanying notes to the financial statements

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN EQUITY: WATER

	For the Fiscal Years Ended June 30,	
	2009	2008
	(in thousands)	
OPERATING REVENUES:		
Residential sales	\$ 32,368	\$ 30,046
Commercial sales	15,928	14,615
Other sales	1,763	1,755
Wholesale sales	802	206
Conservation and Reclamation Programs	934	825
Other operating revenue	3,128	2,408
Total operating revenues before (reserve)/recovery	54,923	49,855
Reserve for uncollectible, net of bad debt recovery	(468)	(252)
Total operating revenues, net of (reserve)/recovery	54,455	49,603
OPERATING EXPENSES:		
Operations	23,647	21,971
Maintenance	5,590	5,540
Purchased energy	4,578	3,650
Purchased water	1,823	2,666
Conservation and Reclamation Programs	441	284
Depreciation	9,771	8,806
Total operating expenses	45,850	42,917
Operating income	8,605	6,686
NON-OPERATING REVENUES (EXPENSES):		
Investment income	3,169	3,357
Interest expense and fiscal charges	(7,049)	(4,401)
Gain (loss) on sale of capital assets	(598)	164
Gain on sale of land	34	12
Other	1,011	1,591
Total non-operating revenues (expenses)	(3,433)	723
Income before contributions and transfers	5,172	7,409
Capital contributions	7,148	18,116
Transfers out - contributions to the City's general fund	(5,276)	(4,955)
Total capital contributions and transfers out	1,872	13,161
Income before special item	7,044	20,570
SPECIAL ITEM:		
Intra-entity property acquisition	(6,388)	-
Increase in equity	656	20,570
EQUITY, BEGINNING OF YEAR	274,487	253,917
EQUITY, END OF YEAR	\$ 275,143	\$ 274,487

* See accompanying notes to the financial statements

STATEMENTS OF CASH FLOWS: WATER

For the Fiscal Years
Ended June 30,
2009 2008
(in thousands)

CASH FLOWS FROM OPERATING ACTIVITIES:

Cash received from customers and users	\$ 54,045	\$ 48,533
Cash paid to suppliers and employees	(37,948)	(31,450)
Other receipts	1,011	1,591
Net cash provided by operating activities	17,108	18,674

CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:

Transfers out - contributions to the City's general fund	(5,276)	(4,955)
Intra-entity property acquisition	(6,388)	-
Principal paid on pension obligation bonds	(98)	(79)
Net cash used by non-capital financing activities	(11,762)	(5,034)

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:

Purchase of utility plant	(37,714)	(42,031)
Proceeds from the sale of utility plant	128	306
Principal paid on long-term obligations	(4,390)	(4,364)
Interest paid on long-term obligations	(6,582)	(3,820)
Proceeds from revenue bonds, including premium	-	120,430
Deposit to escrow account for advance bond refunding	-	(60,300)
Bond issuance costs	-	(1,435)
Capital contributions	11,871	3,531
Net cash provided (used) by capital and related financing activities	(36,687)	12,317

CASH FLOWS FROM INVESTING ACTIVITIES:

Reduction in advances to the City's general fund	-	20
Purchases of investment securities	684	27
Income from investments	3,281	3,080
Net cash provided by investing activities	3,965	3,127
Net increase (decrease) in cash and cash equivalents	(27,376)	29,084

CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR (including \$54,356 and \$14,722 at June 30, 2008 and June 30, 2007, respectively, reported in restricted accounts)

83,933 54,849

CASH AND CASH EQUIVALENTS, END OF YEAR (including \$26,878 and \$54,356 at June 30, 2009 and June 30, 2008, respectively, reported in restricted accounts)

\$ 56,557 \$ 83,933

RECONCILIATION OF OPERATING INCOME

TO NET CASH PROVIDED BY OPERATING ACTIVITIES:

Operating income	\$ 8,605	\$ 6,686
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	9,771	8,806
Amortization of deferred charges-pension costs	77	56
(Decrease) increase in allowance for uncollectible accounts	(86)	87
(Increase) in accounts receivable	(726)	(693)
(Increase) in prepaid expenses	(1)	(4)
(Decrease) increase in accounts payable	(1,095)	2,427
(Decrease) increase in accrued liabilities	(681)	183
Increase in postemployment benefits payable	276	250
Increase in Conservation & Reclamation Programs	23	-
(Decrease) in customer deposits	(66)	(715)
Other receipts	1,011	1,591
Net cash provided by operating activities	\$ 17,108	\$ 18,674

SCHEDULE OF NON-CASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:

Capital contributions - capital assets	3,399	4,706
Decrease in fair value of investments	-	(1)

* See accompanying notes to the financial statements

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Water Utility exists under, and by virtue of, the City Charter enacted in 1883. The Water Utility is responsible for the production, transmission and distribution of water for sale in the City, except for certain areas served by another water utility.

BASIS OF ACCOUNTING

The Water Utility uses the accrual basis of accounting as required for enterprise funds with accounting principles generally accepted in the United States of America as applicable to governments. The accounting records of the Water Utility are also in conformity with the Uniform System of Accounts prescribed by the California Public Utilities Commission. The Water Utility is not subject to the regulations of the California Public Utilities Commission. The Water Utility is not required to and does not elect to implement the pronouncements of the Financial Accounting Standards Board issued after November 1989.

USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during a reporting period. Actual results could differ from those estimates.

REVENUE RECOGNITION

Water Utility customers are billed monthly. Unbilled water service charges are recorded at year-end and are included in accounts receivable. Unbilled accounts receivable totaled \$2,737 at June 30, 2009, and \$2,961 at June 30, 2008.

An allowance for doubtful accounts is maintained for utility and miscellaneous accounts receivable. The balance in this account is adjusted at fiscal year-end to approximate the amount anticipated to be uncollectible.

UTILITY PLANT AND DEPRECIATION

Utility plant assets are valued at historical costs or estimated historical cost, if actual historical cost is not available. Costs include labor; materials; interest during construction; allocated indirect charges such as engineering, supervision, construction and transportation equipment, retirement plan contributions and other fringe benefits. Contributed plant assets are valued at estimated fair value on the date contributed. The cost of relatively minor replacements is included in maintenance expense.

Depreciation is recorded over the estimated useful lives of the related assets using the straight-line method. The estimated useful lives are as follows:

Supply, pumping and treatment plant.....	15-60 years
Transmission and distribution plant.....	25-50 years
General plant and equipment.....	3-50 years

RESTRICTED ASSETS

Proceeds of revenue bonds yet to be used for capital projects, as well as certain resources set aside for debt service, are classified as restricted assets on the Balance Sheets because their use is limited by applicable bond covenants.

In June 2004, the City began collecting a surcharge for water conservation and reclamation programs. This surcharge was approved by the City Council and was phased in over a three-year period with a 0.5%, 1.0% and 1.5% surcharge effective June 1, 2004, 2005 and 2006, respectively. The programs and services offered include conservation, education, and water use efficiency programs; programs to encourage the use of reclaimed water; research, development and demonstration programs to advance science and technology with respect to water conservation and reclamation; and water service provided to low-income customers. This surcharge is scheduled to be in effect for services rendered on or after June 1, 2004 through May 31, 2014. The activity associated with the surcharge for water conservation and reclamation programs is reflected in the accompanying financial statements on the Balance Sheets, Statements of Revenues, Expenses and Changes in Equity, and Statements of Cash Flows.

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

CASH AND INVESTMENTS

In accordance with Water Utility policy, the Water Utility's cash and investments, except for cash and investments with fiscal agents, are invested in a pool managed by the Treasurer of the City. The Water Utility does not own specific, identifiable investments of the pool. The pooled interest earned is allocated monthly based on the month end cash balances.

The City values its cash and investments in accordance with provisions of Governmental Accounting Standards Board (GASB) Statement No. 31, "Accounting and Financial Reporting for Certain Investments and External Investment Pools (GASB 31)," which requires governmental entities, including governmental external investment pools, to report certain investments, at fair value in the Statements of Net Assets/Balance Sheets and recognize the corresponding change in the fair value of investments in the year in which the change occurred. Fair value is determined using published market prices.

Cash accounts of all funds are pooled for investment purposes to enhance safety and liquidity while maximizing interest earnings. Investments are stated at fair value.

City-wide information concerning cash and investments for the year ended June 30, 2009, including authorized investments, custodial credit risk, credit and interest rate risk for debt securities and concentration of investments, carrying amount and market value of deposits and investments may be found in the notes to the City's "Comprehensive Annual Financial Report."

CASH AND INVESTMENTS AT FISCAL AGENTS

Cash and investments maintained by fiscal agents are considered restricted by the Utility and are pledged as collateral for payment of principal and interest on outstanding bonds, or for use on construction of capital assets.

BOND PREMIUM/DISCOUNTS, CAPITAL APPRECIATION, ISSUANCE COSTS, GAINS AND LOSSES ON REFUNDING

Bond premium/discounts, capital appreciation, issuance costs and gains and losses on refunding are deferred and amortized over the term of the bonds using the effective interest method. Bond premium/discounts, capital appreciation, and gains and losses on refunding are presented as a reduction of the face amount of bonds payable, whereas issuance costs are recorded as other assets. Capital appreciation is the annual increase in the value of bonds originally issued at a discounted amount. These bonds do not pay annual interest and mature at a pre-determined par value.

CUSTOMER DEPOSITS

The City holds customer deposits as security for the payment of utility bills. The Water Utility's portion of these deposits as of June 30, 2009 and 2008, respectively, was \$561 and \$626 (including \$109 and \$104, respectively, held on behalf of La Sierra Water Company pending dissolution and distribution of remaining cash asset to shareholders, of which the City is the largest owner).

COMPENSATED ABSENCES

The accompanying financial statements include accruals for salaries, fringe benefits and compensated absences due employees at June 30, 2009 and 2008. The Water Utility treats compensated absences due employees as an expense and a current liability. The amount accrued for compensated absences was \$1,266 at June 30, 2009, and \$1,993 at June 30, 2008, and is included in accrued liabilities in the accompanying Balance Sheets.

Employees receive 10 to 25 vacation days per year based upon length of service. A maximum of two years vacation accrual may be accumulated and unused vacation is paid in cash upon separation.

Employees primarily receive one day of sick leave for each month of employment with unlimited accumulation. Upon retirement or death, certain employees or their estates receive a percentage of unused sick leave paid in a lump sum based on longevity.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

INSURANCE PROGRAMS

The Water Utility participates in a self-insurance program for workers' compensation and general liability coverage that is administered by the City. The Water Utility pays an amount to the City based on actuarial estimates of the amounts needed to fund prior and current year claims and incidents that have been incurred but not reported. The City maintains property insurance on most City property holdings, including Utility plant with a limit of \$1 billion.

City-wide information concerning risks, insurance policy limits and deductibles and designation of general fund balance for risks for the year ended June 30, 2009, may be found in the notes to the City's "Comprehensive Annual Financial Report."

Although the ultimate amount of losses incurred through June 30, 2009 is dependent upon future developments, management believes that amounts paid to the City are sufficient to cover such losses. Premiums paid to the City by the Water Utility were \$380 and \$490 for the years ended June 30, 2009 and 2008, respectively. Any losses above the City's reserves would be covered through increased rates charged to the Water Utility in future years.

EMPLOYEE RETIREMENT PLAN

The City contributes to the California Public Employees Retirement System (PERS), an agent multiple-employer public employee retirement system that acts as a common investment and administrative agency for participating public entities within the State of California.

All permanent full-time and selected part-time employees are eligible for participation in PERS. Benefits vest after five years of service and are determined by a formula that considers the employee's age, years of service and salary. Employees may retire at age 55 and receive 2.7 percent of their highest annual salary for each year of service completed. PERS also provides death and disability benefits. These benefit provisions and all other requirements are established by state statute and City ordinance.

Employee contributions are 8.0 percent of their annual covered salary. The Water Utility is required to contribute the remaining amounts necessary to fund the benefits for its employees using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the PERS Board of Administration. The employer portion of PERS funding as of June 30, 2009 and 2008, was 14.17 percent and 13.29 percent, respectively, of annual covered payroll. The Water Utility pays both the employee and employer contributions. The total Water Utility's contribution to PERS as of June 30, 2009 and 2008, was \$2,138 and \$1,842, respectively.

City-wide information concerning elements of the unfunded actuarial accrued liabilities, contributions to PERS for the fiscal year ended June 30, 2009, and recent trend information may be found in the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2009.

PENSION OBLIGATION BONDS

In 2005, the City issued Pension Obligation Bonds in the amount of \$60,000, of which the Water Utility's share is \$5,890 as reflected in the accompanying Balance Sheet as deferred pension costs and a corresponding long-term obligation. The deferred charge relating to the net pension asset will be amortized over 19 years in accordance with the method used by PERS for calculating actuarial gains and losses. The Bonds will be used to fund the unfunded actuarial accrued liability for non-safety employees and the proceeds were deposited with PERS. The balance in deferred pension costs as of June 30, 2009 and 2008 was \$5,705 and \$5,782, respectively. For more discussion relating to the City's issue, see the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2009.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

OTHER POSTEMPLOYMENT BENEFITS

The City contributes to two single-employer defined benefit healthcare plans: Stipend Plan (SP) and the Implied Subsidy Plan (ISP). The plans provide other postemployment health care benefits (OPEB) for eligible retirees and beneficiaries.

The Stipend Plan is available to eligible retirees and beneficiaries pursuant to their collective bargaining agreements. The Water Utility currently contributes to a bargaining unit through the Service Employee's International Union General Trust (SEIUG). Benefit provisions for the Stipend Plan for eligible retirees and beneficiaries are established and amended through the various memoranda of understanding (MOU). The MOU's are agreements established between the City and the respective employee associations. The City does not issue separate stand-alone financial reports for the plans, instead financial information for the trust funds can be obtained by contacting the individual association.

The Water Utility also provides benefits to retirees in the form of an implicit rate subsidy (Implied Subsidy). Under an implied rate subsidy, retirees and current employees are insured together as a group, thus creating a lower rate for retirees than if they were insured separately. Although the retirees are solely responsible for the cost of their health insurance benefits through this plan, the retirees are receiving the benefit of a lower rate.

The contribution requirements of the Water Utility for the Stipend Plan are established and may be amended through the memoranda of understanding (MOU) between the City and the unions. The Water Utility's contribution is financed on a "pay-as-you-go-basis" and the current contribution is unfunded. The contribution requirements of the Water Utility's Implied Subsidy Plan are established by the City Council. The Water Utility is not required by law or contractual agreement to provide funding other than the pay-as-you-go amount necessary to provide current benefits to eligible retirees and beneficiaries.

The Water Utility's annual OPEB cost (expense) for each plan is calculated based on annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) (UAAL) over a period not to exceed thirty years. The Water Utility's OPEB liability as of June 30, 2009 and 2008 was \$526 and \$250, respectively.

City-wide information concerning the description of the plans, funding policy and annual OPEB cost, funding status and funding progress, and actuarial methods and assumptions for the year ended June 30, 2009 can be found in the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2009.

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

EQUITY

The Water Utility's equity consists of its net assets (assets less liabilities) which are classified into the following three components:

Invested in capital assets, net of related debt – this component consists of capital assets (net of accumulated depreciation) and unamortized debt expenses reduced by the outstanding balance of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted – this component consists of net assets on which constraints are placed as to their use. Constraints include those imposed by creditors (such as through debt covenants), contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or through enabling legislation.

Unrestricted – this component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

CONTRIBUTIONS TO THE CITY'S GENERAL FUND

Pursuant to the City Charter, the Water Utility may transfer up to 11.5 percent of its prior year's gross operating revenues to the City's general fund. In fiscal years ended June 30, 2009 and 2008, the Water Utility transferred 11.5 percent of gross operating revenues, or \$5,276 and \$4,955, respectively.

CASH AND CASH EQUIVALENTS

For the Statements of Cash Flows, cash and cash equivalents include all unrestricted and restricted highly liquid investments with original purchase maturities of three months or less, and all bond construction proceeds available for capital projects. Pooled cash and investments in the City's Treasury represent monies in a cash management pool. Such accounts are similar in nature to demand deposits, and are classified as cash equivalents for the purpose of presentation in the Statements of Cash Flows.

BUDGETS AND BUDGETARY ACCOUNTING

The Water Utility presents, and the City Council adopts, an annual budget. The proposed budget includes estimated expenses and forecasted revenues. The City Council adopts the Water Utility's budget in June each year via resolution.

RECLASSIFICATIONS

Certain reclassifications have been made to prior year's financial statements to conform with the current year's presentation.

PRIOR YEAR DATA

Selected information regarding the prior year have been included in the accompanying financial statements. This information has been included for comparison purposes only and does not represent a complete presentation in accordance with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the government's prior year financial statements, from which this selected financial data was derived.

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 2. CASH AND INVESTMENTS

Cash and investments at June 30, 2009 and 2008, consist of the following (in thousands):

	June 30, 2009	June 30, 2008
	(Fair Value)	
Equity interest in City Treasurer's investment pool	\$ 36,596	\$ 35,688
Investments at fiscal agent	24,691	54,260
	61,287	89,948
Deposits with financial institutions	3,035	2,434
Total cash and investments	\$ 64,322	\$ 92,382

The amounts above are reflected in the accompanying financial statements as:

	June 30, 2009	June 30, 2008
Unrestricted cash and cash equivalents	\$ 29,679	\$ 29,577
Restricted cash and cash equivalents	6,917	6,111
Restricted cash and investments at fiscal agent	27,726	56,694
Total cash and investments	\$ 64,322	\$ 92,382

Cash and investments distribution by maturities as of year end are as follows:

Investment Type	Total	Remaining Maturity (in Months)			
		12 Months or less	13 to 24 Months	25 to 60 Months	More than 60 Months
Held by fiscal agent					
Money market funds	\$ 312	\$ 312	\$ -	\$ -	\$ -
Investment contracts ¹	24,379	19,961	-	-	4,418
City Treasurer's investment pool ²					
Money market funds	4,199	4,199	-	-	-
Federal agency securities	20,155	4,163	3,120	12,872	-
Corp medium term notes	3,166	-	1,065	2,101	-
State investment pool	9,076	9,076	-	-	-
Total	\$ 61,287	\$ 37,711	\$ 4,185	\$ 14,973	\$ 4,418

Presented below is the actual ratings as of year end for each investment type:

Investment Type	Rating as of Year End		
	Total	AAA	Unrated
Held by fiscal agent			
Money market funds	\$ 312	\$ 312	\$ -
Investment contracts	24,379	-	24,379
City Treasurer's investment pool ²			
Money market funds	4,199	-	4,199
Federal agency securities	20,155	20,155	-
Corp medium term notes	3,166	3,166	-
State investment pool	9,076	-	9,076
Total	\$ 61,287	\$ 23,633	\$ 37,654

¹ Amounts related to bond construction proceeds are invested in specific maturities but are available for construction of capital assets as funding is needed.

² Additional information on investment types and credit risk may be found in the City's "Comprehensive Annual Financial Report."

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 3. UTILITY PLANT

The following is a summary of changes in utility plant during the fiscal years ended June 30, 2009 and 2008 (in thousands):

	Balance, As of 6/30/07	Additions	Retirements/ Transfers	Balance, As of 6/30/08	Additions	Retirements/ Transfers	Balance, As of 6/30/09
Source of supply	\$ 32,822	\$ 3,058	\$ -	\$ 35,880	\$ 25,942	\$ (430)	\$ 61,392
Pumping	14,053	4,166	-	18,219	2,563	-	20,782
Treatment	22,697	1,075	-	23,772	-	-	23,772
Transmission and distribution	284,010	27,901	(623)	311,288	16,313	(412)	327,189
General	10,045	2,407	(164)	12,288	1,400	(413)	13,275
Depreciable utility plant	363,627	38,607	(787)	401,447	46,218	(1,255)	446,410
Less accumulated depreciation:							
Source of supply	(10,556)	(610)	5	(11,161)	(779)	33	(11,907)
Pumping	(6,412)	(356)	-	(6,768)	(480)	-	(7,248)
Treatment	(2,404)	(755)	-	(3,159)	(770)	-	(3,929)
Transmission and distribution	(88,453)	(6,251)	487	(94,217)	(6,630)	112	(100,735)
General	(6,365)	(833)	163	(7,035)	(1,112)	414	(7,733)
Accumulated depreciation	(114,190)	(8,805)	655	(122,340)	(9,771)	559	(131,552)
Net depreciable utility plant	249,437	29,802	(132)	279,107	36,447	(696)	314,858
Land	3,923	3,759	-	7,682	3,127	-	10,809
Intangible	5,969	-	-	5,969	46	-	6,015
Construction in progress	27,067	44,888	(40,077)	31,878	41,930	(49,401)	24,407
Nondepreciable utility plant	36,959	48,647	(40,077)	45,529	45,103	(49,401)	41,231
Total utility plant	\$ 286,396	\$ 78,449	\$ (40,209)	\$ 324,636	\$ 81,550	\$ (50,097)	\$ 356,089

NOTE 4. LONG-TERM OBLIGATIONS

The following is a summary of changes in long-term obligations during the fiscal years ended June 30, 2009 and 2008 (in thousands):

	As of 6/30/2007	Additions	Reductions	As of 6/30/2008	Additions	Reductions	As of 6/30/2009	Due Within One Year
Revenue bonds	\$ 95,099	\$ 117,527	\$ (61,716)	\$ 150,910	\$ -	\$ (3,772)	\$ 147,138	\$ 4,415
Pension obligation	5,761	-	(79)	5,682	-	(98)	5,584	119
Postemployment benefits payable	-	250	-	250	276	-	526	-
Water stock acquisition rights	974	-	(10)	964	-	(15)	949	150
Arbitrage liability	416	9	(425)	-	-	-	-	-
Total long-term obligations	\$ 102,250	\$ 117,786	\$ (62,230)	\$ 157,806	\$ 276	\$ (3,885)	\$ 154,197	\$ 4,684

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 4. LONG-TERM OBLIGATIONS *(continued)*

Long-term debt consists of the following (in thousands):

Contracts Payable

	June 30, 2009	June 30, 2008
Water Stock Acquisitions: Payable on demand to various water companies	\$ 949	\$ 964
Total contracts payable	949	964

Revenue Bonds Payable

\$69,840 1991 Water Revenue Bonds: \$25,900 serial capital appreciation bonds due in annual installments from \$3,235 to \$3,240 through October 1, 2010 (partially advance refunded in 1998)

6,475 9,710

\$30,965 1998 Water Refunding/Revenue Bonds: \$15,055 serial bonds due in annual installments from \$315 to \$3,690 through October 1, 2013, interest from 4.70 percent to 5.38 percent; \$10,155 term bonds due October 1, 2018, interest at 5.0 percent; \$5,755 term bonds due October 1, 2027 (partially advance refunded in 2005)

20,405 20,705

\$20,000 2001 Water Revenue Bonds: \$10,070 serial bonds due in annual installments from \$435 to \$585 through October 1, 2016, interest from 3.75 percent to 4.75 percent; \$4,345 term bonds due October 1, 2026 and \$5,585 term bonds due October 1, 2031 were advance refunded in 2005

4,030 4,445

\$60,300 2008 Water Refunding/Revenue Series A Bonds: \$60,300 variable rate bonds due in annual installments from \$425 to \$3,950 from October 1, 2008 through October 1, 2035. Interest rate is subject to weekly repricing (rate at June 25, 2009 was 3.6 percent)

59,875 60,300

\$58,235 2008 Water Revenue Series B Bonds: \$19,890 serial bonds due in annual installments from \$1,210 to \$2,585 from October 1, 2016 through October 1, 2028, interest from 4.0 percent to 5.0 percent; \$11,810 term bonds due October 1, 2033, interest at 5.0 percent; \$26,535 term bonds due October 1, 2038, interest at 5.0 percent

58,235 58,235

Total water revenue bonds payable

149,020 153,395

Total water revenue bonds and contracts payable

149,969 154,359

Unamortized deferred bond refunding costs

(3,101) (3,198)

Unamortized capital appreciation

(427) (938)

Unamortized bond premium

1,646 1,651

Total water revenue bonds and contracts payable, net of deferred bond refunding costs, capital appreciation, and bond premium

148,087 151,874

Less current portion

(4,565) (4,525)

Total long-term water revenue bonds and contracts payable

\$ 143,522 \$ 147,349

Annual debt service requirements to maturity, as of June 30, 2009, are as follows (in thousands):

	2010	2011	2012	2013	2014	2015-2019	2020-2024	2025-2029	2030-2034	2035-2039	Total
Principal	\$ 4,565	\$ 4,615	\$ 4,740	\$ 4,970	\$ 5,200	\$ 21,049	\$ 19,275	\$ 23,160	\$ 28,085	\$ 34,310	\$ 149,969
Interest	5,939	5,892	5,939	5,709	5,289	23,255	19,677	15,675	10,638	4,235	102,248
Total	\$ 10,504	\$ 10,507	\$ 10,679	\$ 10,679	\$ 10,489	\$ 44,304	\$ 38,952	\$ 38,835	\$ 38,723	\$ 38,545	\$ 252,217

NOTE 4. LONG-TERM OBLIGATIONS *(continued)*

The Water Utility's bond indentures require the Utility to maintain a minimum debt service coverage ratio, as defined by the bond covenants, of 1.25. The Water Utility's debt service coverage ratio was 2.25 and 3.88 at June 30, 2009 and 2008, respectively. The debt is backed by the revenues of the Utility (revenue bonds).

PRIOR YEAR DEFEASANCE OF DEBT

In prior years the Water Utility defeased certain Revenue Bonds by placing the proceeds of the new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Water Utility's financial statements. At fiscal year ended June 30, 2009, \$13,320 of bonds outstanding is considered defeased.

2008 WATER REFUNDING/REVENUE BONDS

The City entered into a refunding transaction during the prior fiscal year in response to unusual market conditions brought about by the downgrade of several of the leading municipal bond insurers. These companies provided insurance for the City's Auction Rate Securities ("ARS"). The market that routinely absorbed these instruments through a weekly auction process discontinued their interest in the product and the result was excessively high interest rates, often to the default rate (defined in the bond documents) as the auction "failed," having insufficient bids to clear the auction.

The City's ARS debt was layered with "synthetic fixed rate" swaps designed to maintain the overall cost of funds at a level considered to be in the City's best interest. The unusual market conditions resulted in the swaps not performing as intended and thus the ARS debt was refunded with Variable Rate Demand Notes ("VRDNs"). The notional values of the original swaps remained in place. The transaction was completed (as described below), and the variable rates received on the VRDNs as of June 30, 2009 have resulted in the swaps again functioning as intended, to control the cost of funds on the outstanding variable rate debt.

Because one variable rate debt product was exchanged for another, the typical refunding disclosure measuring the difference in aggregate debt service and calculating an economic gain or loss is less relevant, as the future cash flows of each leg of the calculation are uncertain. For this reason, only the terms of the transaction are described.

On May 7, 2008 \$60,300 of Water Refunding/Revenue Series A Bonds were sold with a true interest cost of 3.22% to refund \$60,300 of previously outstanding 2005 Water Refunding/Revenue Bonds. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$2,905. The difference is being charged to operations using the proportional method. The City completed the refunding to eliminate its investment in ARS and mitigate exposure to the volatile ARS market.

On May 15, 2008, the Water Utility also issued \$58,235 of Water Revenue Series B Bonds to finance additional capital projects of the City's Capital Improvement Program of the Water System. Series B is comprised of: \$19,890 serial bonds, with principal payments from October 1, 2016 through October 1, 2028 ranging from \$1,210 to \$2,585 at interest rates between 4.0 percent and 5.0 percent; \$11,810 term bonds, maturing on October 1, 2033 with interest rate at 5.0 percent; \$26,535 term bonds, maturing on October 1, 2038 with interest rate at 5.0 percent.

INTEREST RATE SWAPS ON REVENUE BONDS

Objective: As a means to lower borrowing costs, when compared against fixed-rate bonds the City entered into interest rate swap agreements in connection with its \$60,300 2005 Water Refunding/Revenue Series A Bonds. The intention of the swap was to effectively change the City's variable interest rate on the bonds to a synthetic fixed rate of 3.20%.

Terms: Under the swaps, the City pays the counterparty a fixed payment as noted above and receives a variable payment computed as 62.68% of the London Interbank Offering Rate ("LIBOR") one month index plus 12 basis points. The swaps have notional amounts equal to the principal amounts stated above. Starting in fiscal year 2009, the notional value of the swaps and the principal amounts of the associated debt decline by \$425 to \$3,950 until the debt is completely retired in fiscal year 2036.

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 4. LONG-TERM OBLIGATIONS *(continued)*

The bonds and the related swap agreements for the 2008 Water Refunding/Revenue Series A Bonds mature on October 1, 2035. As of June 30, 2009, rates were as follows:

Interest rate swap:	Terms	Rates
Fixed payment to counterparty	Fixed	3.20000%
Variable payment from counterparty	62.68 LIBOR + 12bps	(2.50962%)
Net interest rate swap payments		0.69038%
Variable-rate bond coupon payments		2.72754%
Synthetic interest on bonds		3.41792%

Fair value: As of June 30, 2009, in connection with all swap agreements, the transactions had a total negative fair value of (\$4,265). Because the coupons on the City's variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value decrease. The fair value was developed by a pricing service using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement of the swap.

Credit risk: As of June 30, 2009, the City was not exposed to credit risk because the swap had a negative fair value. The swap counterparty, J.P. Morgan Chase Bank was rated A+ by Standard & Poor's. To mitigate the potential for credit risk, the swap agreements require the fair value of the swap to be collateralized by the counterparty with U.S. Government securities if the counterparty's rating decreases to negotiated trigger points. Collateral would be posted with a third-party custodian. At June 30, 2009, there is no requirement for collateral posting for any of the outstanding swaps.

Basis risk: As noted above, the swaps expose the City to basis risk should the relationship between LIBOR and the variable rates converge, changing the synthetic rate on the bonds. If a change occurs that results in the rates moving to convergence, the expected cost savings may not be realized.

Termination risk: The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Schedule to the Master Agreement includes an "additional termination event." That is, a swap may be terminated by the City if the counterparty's credit quality falls below "BBB-" as issued by Standards & Poor's. The City or the counterparty may terminate a swap if the other party fails to perform under the terms of the contract. If a swap is terminated, the variable-rate bond would no longer carry a synthetic interest rate. Also, if at the time of termination a swap has a negative fair value, the City would be liable to the counterparty for a payment equal to the swap's fair value.

NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 4. LONG-TERM OBLIGATIONS *(continued)*

Swap payments and associated debt: As of June 30, 2009, the debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, are summarized as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

Variable-Rate Bonds				
Fiscal Year Ending June 30,	Principal	Interest	Interest Rate Swaps, Net	Total
2010	\$ 425	\$ 1,622	\$ 410	\$ 2,457
2011	450	1,609	407	2,466
2012	800	1,587	402	2,789
2013	825	1,565	396	2,786
2014	850	1,542	390	2,782
2015-2019	5,575	7,306	1,849	14,730
2020-2024	12,700	5,932	1,502	20,134
2025-2029	14,200	4,038	1,022	19,260
2030-2034	16,275	1,943	492	18,710
2035-2036	7,775	108	27	7,910
Total	\$ 59,875	\$ 27,252	\$ 6,897	\$ 94,024

NOTE 5. RESTRICTED EQUITY

Pursuant to applicable bond indentures, a reserve for debt service has been established by restricting assets and reserving a portion of equity. Bond indentures for Riverside's water revenue bonds require reserves that equate to the maximum annual debt service required in future years plus three months interest and nine months principal due in the next fiscal year. The 2008 Refunding/Revenue Series A Bonds require 110% of the monthly accrued interest be included in the reserve. Additional reserves for the 2008 Revenue Series B Bonds and the 1998 Revenue Bonds are not required due to the purchase of surety bonds to cover the reserve requirements.

NOTE 6. LITIGATION

The Water Utility is a defendant in various lawsuits arising in the normal course of business. Present lawsuits and other claims against the Water Utility are incidental to the ordinary course of operations of the Water Utility and are largely covered by the City's self-insurance program. In the opinion of management and the City Attorney, such claims and litigation will not have a materially adverse effect upon the financial position or results of operation of the Water Utility.

The Water Utility is also a plaintiff in a lawsuit against the manufacturers and distributors of methyl tertiary-butyl ether (MTBE) and its by-products, and of fuel containing these chemicals, arising out of the threat to the Water Utility wells of contamination with those chemicals from leaking underground storage tanks.

The defendants removed this lawsuit to federal court and then transferred the case to the Judicial Panel on Multidistrict Litigation, New York, where it was consolidated with all other pending MTBE water contamination litigation cases in the country. Although the City has tentatively settled with a number of the defendants, the settlement has not been approved by the court and there is no trial date for the remainder of the case.

NOTE 7. CONSTRUCTION COMMITMENTS

As of June 30, 2009, the Water Utility had major commitments of approximately \$8,663 with respect to unfinished capital projects, of which \$8,000 is expected to be funded by bonds and \$663 funded by rates.

NOTE 8. SPECIAL ITEM

On December 6, 2005, the City Council adopted a resolution approving a fair market value transfer to the General Fund of approximately 190 acres out of a 227-acre parcel owned by the Utility's Water Fund. The transfer was facilitated by a loan from the Electric Fund to the General Fund. The transfer was intended to assist in the collaborative development of the property in conjunction with other entities, which have now been hampered by the current economic downturn that is particularly impacting the construction industry.

On June 16, 2009, the Water Utility reacquired the 190-acres from the City and rescinded the original transaction. The City's Water Utility desires to improve its groundwater resources which are critically important to avoid dependence on high-priced imported water. The Utility anticipates using the property for projects such as water production and groundwater replenishment facilities that will be critical to the City's use of the Riverside Groundwater Basin.

The Utility reacquired the land for a price of \$8,980. The original and current carrying value of the land in the Water Utility's capital assets remains at \$2,592. The balance between the purchase price and the carrying value of \$6,388 is recorded as a special item.

KEY HISTORICAL OPERATING DATA: WATER

WATER SUPPLY *(acre feet)*

	2008/09	2007/08	2006/07	2005/06	2004/05
Pumping	76,830	80,974	85,299	76,605	73,732
Purchases	0	1,643	2,092	2,670	4,137
Total:	76,830	82,617	87,391	79,275	77,869
Percentage pumped	100.00%	98.0%	97.6%	96.6%	94.7%
System peak day (gallons)	105,780,000	111,300,000	109,200,000	118,782,000	112,094,000

WATER USE

	2008/09	2007/08	2006/07	2005/06	2004/05
Number of meters as of year end					
Residential	58,152	57,694	57,666	57,308	56,916
Commercial/Industrial	5,519	5,446	5,279	5,204	5,114
Other	391	354	486	473	462
Total:	64,062	63,494	63,431	62,985	62,492
*CCF sales					
Residential	17,898,798	18,483,522	19,848,653	17,702,717	17,245,315
Commercial/Industrial	10,342,284	10,510,953	10,817,783	9,822,196	9,252,639
Other	983,553	970,239	1,243,927	1,157,130	1,199,448
Subtotal:	29,224,635	29,964,714	31,910,363	28,682,043	27,697,402
Wholesale	496,601	618,552	199,845	182,987	177,851
Total:	29,721,236	30,583,266	32,110,208	28,865,030	27,875,253

*(CCF equals 100 cubic feet)

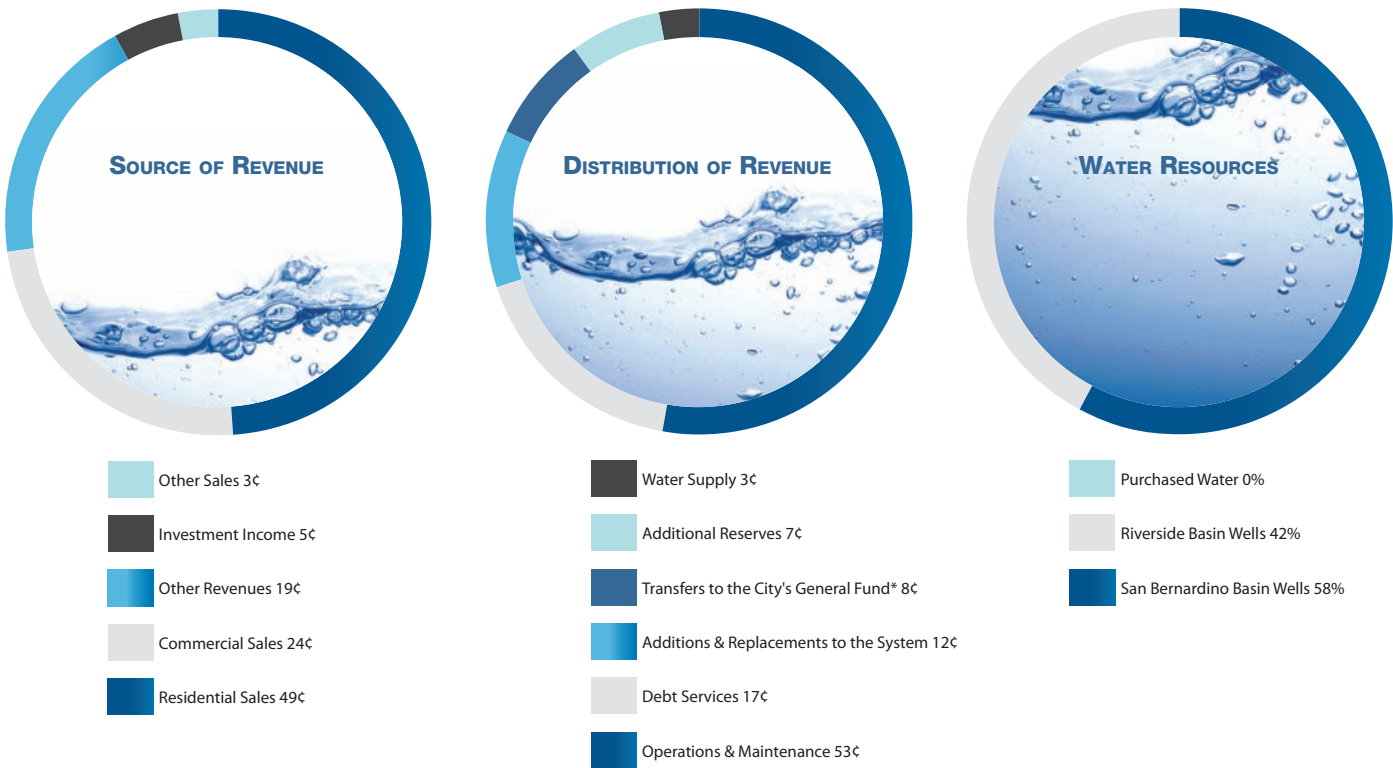
WATER FACTS

	2008/09	2007/08	2006/07	2005/06	2004/05
Average annual CCF per residential customer	308	320	345	312	308
Average price (\$/CCF) per residential customer	\$1.80	\$1.63	\$1.43	\$1.26	\$1.16
Debt service coverage ratio	2.25	3.88	3.38	5.11	2.85
Employees ¹	167	167	165	137	130

¹Approved positions

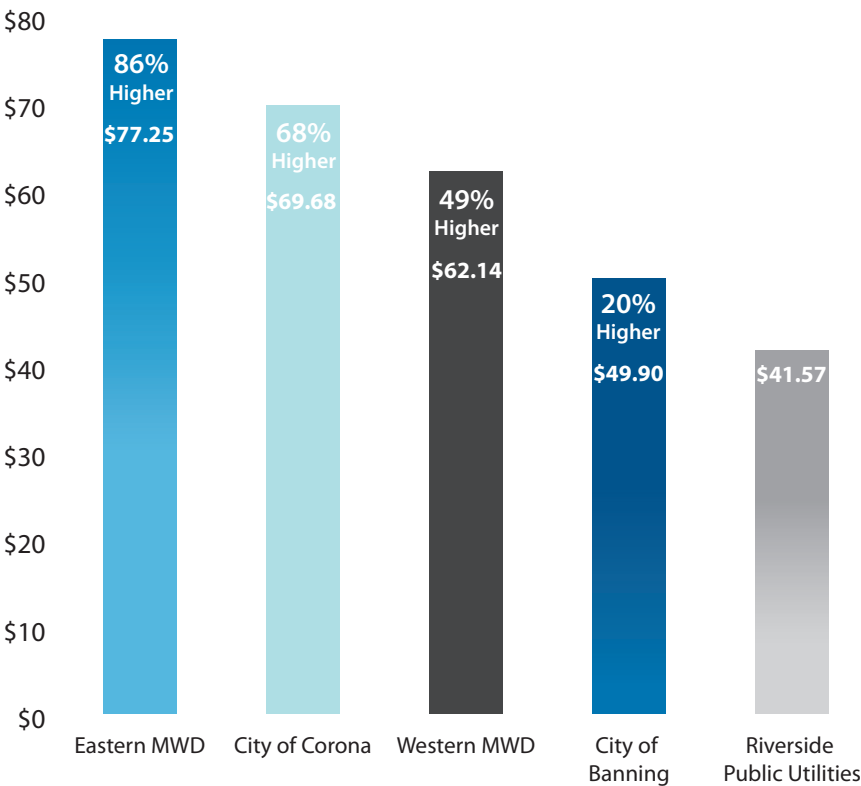
KEY HISTORICAL OPERATING DATA: WATER

2008/2009 WATER REVENUE AND RESOURCES



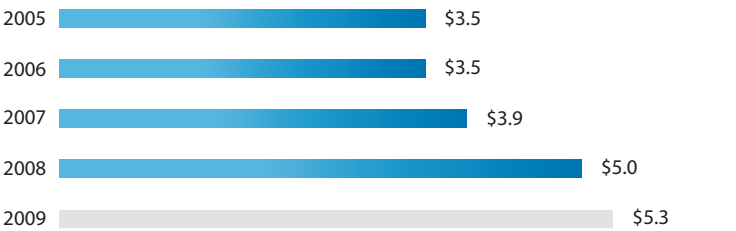
* BASED ON TRANSFER OF 11.5% OF FISCAL YEAR 2007/2008 REVENUES.

RESIDENTIAL WATER RATE COMPARISON – 26 CCF PER MONTH (AS OF JUNE 30, 2009)

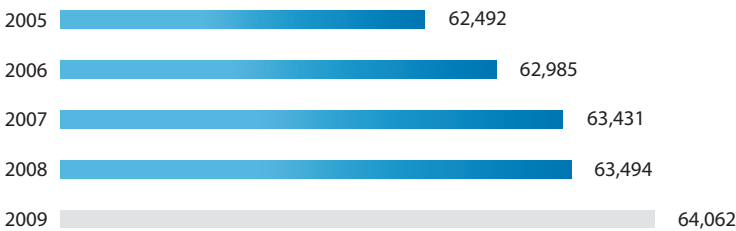


KEY HISTORICAL OPERATING DATA: WATER

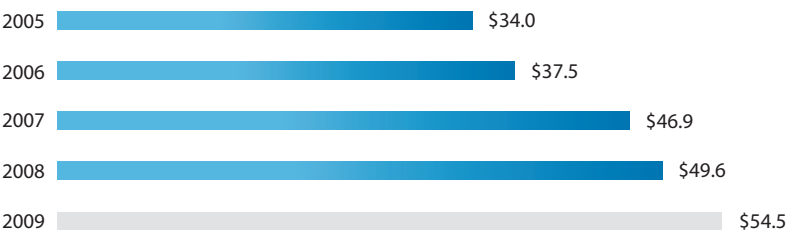
GENERAL FUND TRANSFER *(in millions)*



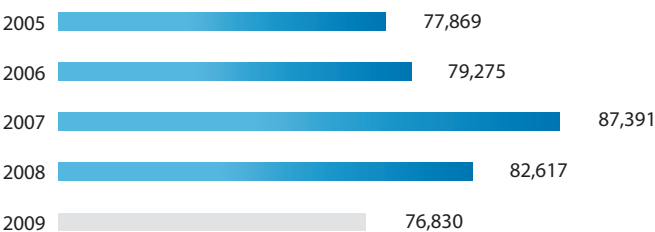
NUMBER OF METERS AT YEAR END



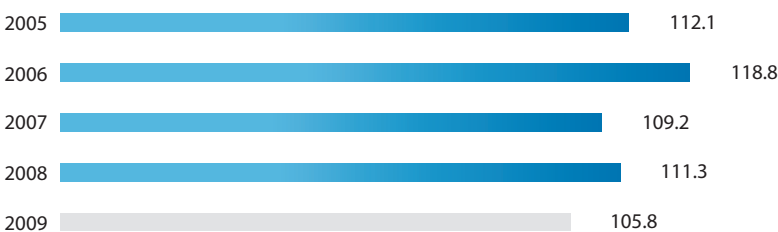
TOTAL OPERATING REVENUE *(in millions)*



PRODUCTION *(in acre feet)*



PEAK DAY DEMAND *(in million gallons)*



WATER FACTS AND SYSTEM DATA

Established	1913
Service Area Population	300,430
Service Area Size (square miles)	73.8
System Data:	
Smallest pipeline	2.0"
Largest pipeline	72.0"
Miles of pipeline	993
Number of domestic wells	55
Number of active reservoirs	15
Total reservoir capacity (gallons)	99,990,000
Number of treatment plants	7
Number of treatment vessels	99
Miles of canal	14
Number of fire hydrants	7,523
Daily average production (gallons)	68,812,439
2008-2009 Peak day (gallons):	105,780,000
7/2/08, 101 degrees	
Historical peak (gallons):	118,782,000
8/9/05, 99 degrees	

BOND RATINGS

FITCH RATINGS	AA
STANDARD & POOR'S	AA+